



STATE OF CALIFORNIA
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DEPARTMENT OF CORPORATIONS
California's Investment and Financing Authority
NEWS RELEASE

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Arnold Schwarzenegger, Governor

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FOR IMMEDIATE RELEASE

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California Issues
“Dirty Dozen” Investment Scams for 2005

Sacramento, February 2, 2005 – The California Department of Corporations (Corporations), California's securities regulator, today issued a list of its “Dirty Dozen” Investment Scams for 2005 and a warning to investors to thoroughly investigate new investment opportunities before handing over their money.

“These schemes offer products and pitches with unrealistically high returns that may sound tempting to many investors,” said Corporations Commissioner William P. Wood. “If the investment opportunity sounds too good to be true, it usually is,” Wood added.

The North American Securities Administrators Association has alerted investors to scams that are commonly seen throughout the United States, and Corporations wants investors to be aware of the most prevalent schemes that harm both consumers and legitimate investment businesses in California.

Corporations advises potential investors to protect themselves from becoming victims of fraud by doing their homework before making an investment. Investors can contact Corporations before they invest to check the registration status of the investment they are considering and/or the licensing status of the person who is selling it through a toll-free telephone number, 1-866-ASK-CORP (1-866-275-2677).

The following is the list of Corporations’ “Dirty Dozen” Investment Scams for 2005 in California:

- 1. Senior Investment Fraud.** Low interest rates, rising health care costs and an increased life expectancy have set seniors up as targets for con artists peddling investment fraud, including promissory notes, charitable gift annuities and viatical settlements. Seniors are particularly targeted because they often have access to a large amount of assets as a result of a lifetime of savings and buildup of home equity.
- 2. Variable Annuities Sales.** As sales of variable annuities have risen, so have complaints from investors—most notably, the omission of disclosure about costly surrender charges and steep sales commissions. These surrender charges and high fees combine with other factors to make variable annuities inappropriate for many investors, particularly for purchases in retirement accounts. Most recently, Corporations launched a sweep of broker-dealer offices statewide to weed out fraudulent sales practices of variable annuities.

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3. Charity/Tsunami Scam. Con artists often try to make money out of tragedy. There may be con artists attempting to collect money under the guise of being involved in the tsunami relief effort or by offering phony bonds to finance the reconstruction of areas affected by the disaster. Donors need to check out the charity carefully, demand details, beware of excessive pressure, and make sure any donations are tax deductible. E-mail scammers are sending out pleas for help from phony survivors, invading recipients' computers and stealing financial and other information from those who click on links in the documents.

4. Ponzi/Pyramid Schemes. Typically an unknown company is offering eye-popping returns from some plausible sounding, but vaguely described business activity. Such schemes are often spread by word of mouth through groups such as churches, ethnic groups, or professional affiliations, frequently in an atmosphere of secrecy. The formula is simple: Promise high returns to investors and use their money to pay previous investors.

5. Military Fraud. Predatory salespeople target military recruits and active military service personnel who are misled into purchasing unsuitable investment products. The NASD, together with the SEC, recently settled a major mutual fund practice case against a firm that specialized in selling expensive systematic investment plans to military personnel. The firm agreed to pay \$12 million following findings that the plans were sold in a misleading fashion. The fines will be used for restitution to affected investors with the balance used for investor education for the U.S. military and their families.

6. Viatical Settlements. One of the riskiest investment products, viatical contracts are interests in the death benefits of life insurance policies. Investors get a share of the death benefit when the insured later dies, after a fee is paid to the viatical investment broker. These investments are extremely risky for numerous reasons, including difficulty predicting life expectancy, the promoter not paying policy premiums as promised, or the promoter simply stealing the investor's money. Last year, Corporations obtained a judgment of \$20 million against a fraudulent viatical investment firm in San Diego.

7. Living Trust Mills and Other Pretext Solicitations to Seniors. Corporations' SAIF (Senior Against Investment Fraud) program regularly receives large numbers of complaints from the elderly on living trust mills. The initial approach to clients may be to solicit seniors at "seminars" purportedly designed to educate participants about the benefits of living trusts or other estate planning subjects such as Medi-Cal planning or general financial planning. These seminars misrepresent the actual business of the sales representative and the true purpose of the solicitation. The real goal of the sales agent is to obtain detailed personal financial information, which will then be used to sell the senior an unsuitable or unlawful financial or investment product.

8. Bait and Switch Schemes. Investors should be very wary about advertising in which a particular investment promises spectacular profits, but investors have to be lured into the office to get it. This is the bait. Once in the office to purchase the investment, the sales agent discourages the investor from investing in the advertised product. The sales agent then switches an investor into a different investment.

9. Affinity Group Fraud. Members of closely-knit religious, ethnic, and cultural groups are targeted by con artists who share or claim to share their characteristics or interest. In an Asian community in California, a finance lender charged in excess of 200 percent interest in some cases.

10. Wrong Numbers and Stock Tips Scam. Some people are finding that they have received a “misdialed” call from a stranger, leaving a “hot” investment tip for a friend. The message is designed to sound as if the caller didn’t realize that he or she was leaving a hot stock tip on the wrong message machine. Con artists have also sent these fraudulent messages through e-mails and faxes.

11. CD + Bonuses. Scammers promise investors tantalizingly high rates of return on investments by including a bonus payment to attract investors. In an enforcement action brought by Corporations, a firm offered one-year certificates of deposits (CDs) that were purportedly FDIC-insured with yields substantially higher than those actually available from any actual FDIC-insured institution. The firm paid the bonus out of its own pocket; investors were tricked into sales of annuities.

12. Online Escrow Fraud. Purchases through online auction sites such as eBay have become a popular arena for fraud. Online escrow services are often used for expensive online purchases such as computers, electronics, jewelry, and cars. Legitimate online escrow companies act as a neutral third party that holds payment for merchandise until the buyer receives the merchandise. However, a fraudulent escrow company will lure unsuspecting buyers or sellers to transact business through their Web site and then keep the funds and/or goods.

In an effort to combat online escrow fraud, Corporations has issued Desist and Refrain orders to 41 Internet escrow providers since spring 2004 to shut down fraudulent escrow sites and formed the Escrow Fraud Task Force, a collaboration of state and federal regulators, law enforcement, industry groups, and businesses.

The Department of Corporations is California's Investment and Financing Authority. Corporations is responsible for the regulation, enforcement and licensing of securities, franchises, off-exchange commodities, investment and financial services, independent escrows, consumer and commercial finance lending and residential mortgage lending. For further information or to obtain a complaint form, please visit Corporations’ Web site at www.corp.ca.gov or call 1-866-ASK-CORP (1-866-275-2677).

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